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SUBJECT: South Africa: Minerals and Energy Newsletter "THE ASSAY" - Issue 3, 16-29 February, 2008

This cable is not for Internet distribution.

¶1. (SBU) Introduction: The purpose of this newsletter, initiated in January 2004, is to highlight minerals and energy developments in South Africa. This includes trade and investment as well as supply. South Africa hosts world-class deposits of gold, diamonds, platinum group metals, chromium, zinc, titanium, vanadium, iron, manganese, antimony, vermiculite, zircon, alumino-silicates, fluorspar and phosphate rock, and is a major exporter of steam coal. South Africa is also a leading producer and exporter of ferroalloys of chromium, vanadium, and manganese. The information contained in the newsletters is based on public sources and does not reflect the views of the United States Government. End introduction.

HOT NEWS

France's Nuclear Charm Offensive

¶2. (SBU) French President Nicholas Sarkozy, accompanied by his wife, led a senior commercial delegation of 40 business people on a two-day state visit to South Africa during February 28-29. The President signed a number of cooperation agreements with the SAG and handed out a package of monetary and technical assistance incentives in support of French company Areva's bid for large nuclear contracts. Their competitor is U.S. company Westinghouse. The French President hoped to help secure South Africa's lucrative long-term fleet of new nuclear build and his timing was impeccable as the closing date for the tender submission for the first 3,500 megawatt tranche of new build was January 31. The initial evaluation of the bids from Areva and Westinghouse was done on February 15 and Eskom's board is due to give its recommendation on the preferred vendor by June after receiving final bids on March 31. The final decision will be made by parliament and will include soft issues that contribute 20 percent to the scoring of the tenders. They soft issues deal with social, labor and technology transfer spin-offs that are important to the SAG's transformation and upliftment goals.

¶3. (SBU) The first tranche, known as Nuclear 1, is for the

construction of a nuclear power plant (with two to three individual reactor units) with capacity between 3,000-3,500 megawatts ($16 billion). The grand prize however will be the tender for a 20,000 megawatt fleet of nuclear plants by 2025 ($100 billion). The French are pulling out all the stops to win these contracts. They believe they have the advantage because they built South Africa's only nuclear plant in the Western Cape, the twin-unit 1,800 megawatt Koeberg facility that has operated successfully for more than 20 years. Areva also stepped in to provide a replacement rotor when one of the Koeberg units was damaged in a freak accident in 2006. Westinghouse believes that their newer more flexible reactor technology and their proven ability to technically empower local people to manufacture, build and operate nuclear plants through training and technology transfer, as they did in France and have Qmost
recently done in South Korea, will swing both the technical and political decisions in their favor.

EXPLORATION

Exploration Boom for Tomorrows Metals

¶4. (SBU) The Metals Economics Group says that global exploration is alive and well. Expenditures have increased by more than 450 percent since the nadir of 2002 when a total of only $1.9 billion was spent on exploring for non-ferrous minerals. The amount spent in 2007 was $11.4 billion. Most exploration is carried out by small and junior companies that generally sell finds to major mining companies in order to maintain their cash flows. Juniors accounted

for more than 53 percent, intermediaries 16 percent and majors 31 percent of exploration expenditures. In terms of where the money was spent, 24 percent went to Latin America, 19 percent to Canada, 16 percent to Africa, 12 percent to Australia, 8 percent to the United States, 4 percent to Pacific/SE Asia and 17 percent to the rest of the world. The commodity split heavily favored the precious minerals with 42 percent going to gold, 36 percent to base metals, 10 percent to diamonds, 3 percent to platinum group metals (PGMs), and 9 percent for others

¶5. (SBU) The African tranche of exploration expenditures went mainly to South Africa, DRC, Angola, Tanzania, Botswana and Ghana, with South Africa taking 4 percent of the global figure. Exploration in South Africa was focused on PGMs in the Bushveld Complex, but gold and diamonds also featured strongly. This exploration took place despite concerns about government policies and the prevailing electricity shortage, which casts doubt on Eskom's capacity to supply new mines for the next few years. Diamonds dominated exploration in the DRC and Angola and there was also significant activity in the DRC/Zambian copper-cobalt belt that straddles the border between the two countries. The DRC government's review of all exploration leases and mining contracts has sent a wave of uncertainty through the mining community that could impact on further investment until the matter is resolved. Copper and uranium were the main targets in Zambia, gold in Tanzania and Ghana, uranium and diamonds in Namibia, and diamonds, copper, nickel and coal in Botswana. Botswana is already the world's biggest diamond producer and appears destined to become prominent in coal where resources are estimated to exceed 200 billion tons of steam coal. A number of other African countries have on-going exploration programs for a variety of minerals and oil and gas.

ELECTRICITY

Saving Power in SA

¶6. (SBU) South Africans are thought to use energy very inefficiently

and some experts believe that a 30 percent to 50 percent reduction in household use is attainable. Eskom made a plea to residential consumers in a recent three-page Sunday newspaper advertisement to adopt conservation and efficiency measures because the country no longer had the luxury of excess capacity and will have to embrace energy efficiency as a way of life. Eskom said the situation would remain tight for the next five years until new build comes on line, and also outlined its National Response Plan for mitigating and resolving the power shortage.

¶7. (SBU) The National Response Plan identifies three phases:
-- Phase 1 - Stabilization (generally completed). A 10 percent reduction in power consumption has been imposed on mining and industrial consumers and coal stock-piles have been replenished. (The power allocation to mines has subsequently been increased to an average of 95 percent.)
-- Phase 2 (March-July). A 10 percent across-the-board power reduction will be applied to municipalities. Eskom intends to Qreduction will be applied to municipalities. Eskom intends to monitor progress during this time. (Eskom has also threatened to re-impose load-shedding on residences, absent adequate conservation gains.)
-- Phase 3 - Power conservation (next four years) and fast-tracking new power build, while sustaining the power reduction to enable growth and assure operational reserves.

MINING

SA Mines Expansion Stymied by Power Crisis

¶8. (SBU) Chamber of Mines executive Frans Barker says that the recent decision by Eskom to increase the average power supply to mines to 95 percent is welcomed and will save jobs, but it will not

be enough for the sector's expansions plans. Mining created 40,000 new jobs last year. Barker said some mines might not receive more than 90 percent power and others could receive their full requirement where the 10 percent reduction would impact heavily on jobs. Whatever the split, therewould still be some losses in jobs and production in the short term. In the longer-term, the mines can probably adjust to the reduced power levels. Barker said the biggest concern was that many projects in the pipeline would likely be delayed or shelved, and there was an urgency to develop a strategy to mitigate these effects in the medium term. BHP-Billiton has announced that it plans to reduce aluminum production by 120,000 tons a year from its southern African smelters (15 percent of total output valued at $500 million at current metal prices) due to Eskom's power rationing.

Post Boom SA Mining - Where To?

¶9. (SBU) A Business Day editorial writer lamented that increasing state bureaucracy, intervention, and politicization of the business process is "poisoning South African business". He cited the increasing scope of state licensing required to carry out business and noted that mining licensing requirements are now so onerous that although South Africa has some of the most attractive mining assets in the world, its mining sector is being stifled by excess government regulation. This was especially unfortunate during the current super commodity boom, according to the writer. Thousands of exploration and mining license applications await processing by the Department of Minerals and Energy (DME), but the ministry lacks the capacity and experience to process them. Booming commodity prices have given the industry respectable financial returns, but little increase in production. In other words, mining is doing well, but it could be doing a great deal better if the state would step aside and allowed miners to work. The real question is what will happen if the boom comes to an end and prices return to their earlier levels? Investors would again be able to pick and choose from a range of global projects and South Africa may be low on their

investment list. Under these circumstances, could marginal mines survive, would the low level of exploration have produced new mines, and would new investment be available to fund expansions to existing mines or bring new mines on stream?

¶10. (SBU) This uncertainty was exacerbated when the newly elected ANC Secretary-General Gwede Mantashe hinted at the creation of more state-owned enterprises in the resource sector after the country's upcoming elections in 2009. Speaking at a Centre for Development and Enterprise function in Johannesburg, Mantashe argued for greater state intervention in the economy. He targeted the commodity sector in general, and platinum mining in particular but stressed that he was not talking nationalization but rather partnerships with private companies in productive enterprises. He said this would accelerate Qcompanies in productive enterprises. He said this would accelerate the release of mineral rights and create new financial resources for wealth redistribution. He noted that such models were common in other parts of the world, including neighboring Botswana and Namibia where the states are in 50/50 partnerships with De Beers in diamond mining. Mantashe's comments were made as platinum jumped to a new record high of above $2,200 per ounce on supply fears resulting from electricity rationing at South African mines.

BOTSWANA

Mining Industry Booming

¶11. (SBU) Prior to the discovery of diamonds, Botswana was a poor country that relied heavily on cattle ranching, subsistence agriculture, and assistance from the British government for economic survival. Some gold, copper-nickel, potash and coal mining was active but their combined contribution to the economy was small. Discovery of the world's richest diamond pipes at Orapa and Jwaneng in the 1960's and 1970's changed all that and, together with good

governance and an investor-friendly fiscal regime, the country has prospered. Diamonds have accounted for a major portion of the country's exports and GDP over the past two decades and the GOB is seeking to diversify the economy away from its reliance on a single commodity. Botswana's enlightened mining code has encouraged exploration and the country has experienced a resurgence of exploration and mining activity over the last couple of years. Exploration is continuing for a wide variety of minerals and several new projects were launched during 2007. Recent discoveries include new deposits of diamonds, coal, gold, uranium, copper-cobalt, nickel, and coal-bed methane.

¶12. (SBU) Projects underway and planned include moving the headquarters of the Diamond Trading Company (DTC), De Beers' rough diamond marketing arm, from London to Botswana. The DTC should be operational by the end of the year and has agreed to sell $360-million worth of rough diamonds to Botswana gem cutters to create some 3,000 jobs. A number of new diamond mining developments are underway, which should add another one million carats per year by 2012. The government is also making progress in promoting local mineral beneficiation with metal refiner Activox to produce finished copper and nickel cathodes in Botswana. At peak construction, the project is expected to employ more than 4,000 people. There are also plans to construct a third diamond plant at Orapa and to start underground mining at Jwaneng. Botswana's huge coal resources, estimated at more than 200 billion tons, are of major interest to an energy-short South Africa. Canadian CIC Energy Corporation is planning to build a $5.5 billion, 3,600 megawatt coal-fired power station to supply energy to South Africa and the plant is scheduled for commissioning in 2011. The potential for coal-bed methane is also being investigated.

IN BRIEF

SA Gold Dominance Ends

¶13. (SBU) South Africa has been the world's major gold producer since 1905 (when it overtook the U.S.), reaching a peak output of 1,000 tons in 1970. Since then, updated output figures show that production declined by 7.4 percent in 2007 to 254.7 tons (8.19 million ounces), and estimates are for a further 10 percent decline in 2008 due to power shortages. At the same time Chinese output increased to between 270 and 276 tons, making them the world's number one producer. Australia and the United States occupied third and fourth positions with 248 and 240 tons, respectively, although both countries saw a slight decline in annual output.

Iran to Invest in Zimbabwean Oil Refinery

¶14. (SBU) The state-controlled Zimbabwean Herald has reported that the Iranian Ambassador to Zimbabwe said his country plans to invest in rehabilitating Zimbabwe's Feruka Oil Refinery. The refinery is located in the eastern city of Mutare (previously Umtali), located near the border with Mozambique. It is connected by pipeline to the
Qnear the border with Mozambique. It is connected by pipeline to the
Mozambican port city of Beira from where most of Zimbabwe's fuel supplies are pumped. The Ambassador said that Iranian technical teams had evaluated the plant, and had submitted their findings to the respective Governments, which were negotiating legal and other issues.

Coal Use could Increase by 73 percent

¶15. (SBU) At a recent energy conference in Johannesburg, the CEO of business strategy consultancy firm Stratek said that over the next 25 years global coal use is set to increase by 73 percent, overall energy demand by 50 percent, and oil demand to 116-million barrels a day (from the current 82 million barrels). He said that coal's

current share of the energy mix was 25 percent in 2005, but this would rise to 28 percent by 2030.

Viable Uranium Price is $120 per Pound

¶16. (SBU) Speaking at a uranium conference in Johannesburg, Witwatersrand University Geosciences Professor Judith Kinnaird said that the current price of uranium would have to be $120 per pound (currently below $70) to be equivalent to the price two decades ago. She said that the 439 nuclear reactors operating in 41 countries currently produced 16 percent of the world's electricity. She also said that 34 reactors were in construction, 93 were on order or planned, and 222 were being proposed.

BOST